BEFORE
THE PUBLIC SERVICE COMMISSION OF SOUTH CAROLINA

KIAWAH ISLAND UTILITY, INC.
DOCKET NO. 96-168-W/S

TESTIMONY
OF
PHILIP E. MILLER

RETURN DATE: ________
SERVICE: OK ________

ON BEHALF OF
THE DEPARTMENT OF CONSUMER AFFAIRS

NOVEMBER 18, 1996

Introduction

Q. Would you please state your name?
A. Philip E. Miller.

Q. What is your business address?
A. My business address is Riverbend Consulting, 1750 Flinthill Drive, Columbus, Ohio 43223.

Q. Would you please highlight the history of your past employment and education?
A. I have over twenty-nine years experience in the utility field. During this period, I was employed four years by utility companies, six years with the Public Utilities Commission of Ohio, and three years with the Ohio Consumers' Counsel. For the last sixteen years, I have operated or been employed by an independent consulting firm.

I have served both as a Chief Accountant to a regulatory agency and as Technical Advisor to a consumer advocate. My qualifications and experience are presented in Appendix 1 to my direct testimony.

Q. Have you ever presented direct expert testimony in rate proceedings?

A. Yes, I have. I estimate that I have testified in over 300 rate proceedings. Testimony has been presented in the states of Arizona, California, Florida, Hawaii, Indiana, Louisiana, Maine, New Mexico, Ohio, Rhode Island, South Carolina, Texas, Washington, and West Virginia.

Q. Have you ever presented direct testimony before this Commission?

A. Yes, I have testified a number of times before this Commission. This includes testimony in a number of water and sewer proceedings.

Q. What is the purpose of your testimony?

A. I have been retained by the Consumer Advocate to analyze the Company's application for an increase in rates and charges, and in particular to analyze and review all issues which affect operating income and rate base. Subsequent to this review, I have been asked to provide the Commission with my position concerning the various operating income and rate base issues. This testimony sets forth the aforementioned analysis and recommendations.

My testimony also presents the Commission with the Consumer Advocate's revenue requirement recommendation.

Q. What documents have you reviewed in the preparation of your testimony?

A. I have reviewed Company testimony and exhibits, responses to discovery, Company workpapers, responses to Staff data requests, certain PSC Opinions and Orders, and other documents and data.

Q. Would you please summarize your testimony?

A. My testimony addresses the following issues:

1) Professional fees
2) Legal fees
3) Management fee
4) Rate case expense
5) Repair and maintenance expense
6) Sludge removal adjustment
7) Depreciation expense adjustment
8) Interest synchronization
9) Rate base
10) Customer Growth

Revenue Requirements

Q. What is your recommendation concerning the Company's proposed revenue increase?

A. My revenue requirement recommendation is based on the operating margin methodology because the Commission typically uses it to determine revenue requirements for water and sewer utilities whose rate base has been substantially reduced by contributions in aid of construction and other non-investor sources of funds. However, it was necessary to determine an appropriate rate base in order to compute the interest which should be considered when developing the operating margin.

Schedule 1 illustrates the adjusted operating margin which results from the recommendations contained in my testimony. As illustrated, the adjusted operating margin for the test year is 6.98%. Based on this operating margin, it is my recommendation that the Company's proposed increase in rates be rejected by the Commission.

Q. Why is your adjusted operating margin, not only a positive one, but also significantly higher than the Company's?

A. There are two primary reasons, both of which I discuss in more detail in the ensuing testimony. First, the test year operating expenses contained a number of unusual and extraordinary items which need to be normalized for ratemaking purposes. Second, the Company's interest expense recommendation is based upon significant additions to rate base which should not be considered in this proceeding.

Professional Fees

Q. What is the Company's position pertaining to its professional fees?

A. The test year professional fees (which the Company also refers to as consulting fees) amounted to $101,254. The Company is proposing to eliminate $46,790 of this amount in order that the professional fees for ratemaking purposes will be based upon an average of the professional fees incurred during the three year calendar period of 1993 through 1995.

Q. What is your position regarding the Company's proposed adjustment?

A. The Company's adjustment is certainly a step in the right direction. It is obvious looking at the Company's professional fee history that an adjustment is in order. In this regard, although the test year fees amounted to $101,254, the fees for 1994 and 1993 amounted to $58,004 and $4,135 respectively. Therefore, unless the test year amount is adjusted, the Company's revenue requirements would be based upon an abnormally high expenditure that the Company can not anticipate incurring in future years. However, it is my position that the Company's adjustment does not eliminate enough of the abnormality, and that an additional decrease in the test year professional fees is in order.

Q. Why do you believe that an additional adjustment is in order?

A. The Company's proposed adjustment does not consider the specific unusual and extraordinary consulting fees which were incurred during the test year. When these specific unusual and extraordinary fees are considered, and then amortized, a greater reduction will result than that proposed by the Company.

Q. Would you please explain these unusual and extraordinary fees to which you refer?

A. According to the Company's responses to Consumer Advocate Interrogatories 2-9 and 2-10, a large fire destroyed two houses on Kiawah on July 20, 1994. Because of this fire, questions were raised by the Town of Kiawah and St. John's Fire Department about the adequacy of KIU's water system to provide sufficient flow of water in the event of an emergency. Although the Company did not believe that these concerns were valid, nevertheless they hired Gage-Babcock to perform an independent study of its water system, and to respond to numerous questions that were raised. Gage-Babcock produced a report entitled "Fire Protection Engineering Report/Kiawah Island/Charleston, SC" in October 1994. A copy of this report is attached to the Company's response to Consumer Advocate Interrogatory No. 2-9c.

In addition to conducting this study and participating in a Task Force which included other consultants hired by the Town of Kiawah and St. Johns, Gage-Babcock also assisted KIU in the analysis of proposed ordinances of the Town of Kiawah Island relating to fire flows.

According to the Company, it has incurred the following costs in connection with the fire related studies conducted by Gage-Babcock:

1994	$17,453
1995	$40,035
1996	$ 2,301

Obviously, these consulting fees are unusual and extraordinary because they relate to studies which cannot reasonably be expected to be incurred again in the near future. As such, an argument could be made for complete exclusion of the test year amount. Yet, it is my recommendation that instead the test year costs associated with these consulting fees be amortized over a five year period. This will allow the Company to recover these costs it incurred for this safety measure, but at the same time it will not over burden the ratepayers with this unusual and extraordinary cost. As shown on Schedule 3, this adjustment will reduce the Gage-Babcock test year consulting fees by $32,028.

However, the fees paid to Gage-Babcock were not the only consulting fees associated with these fire studies. I have attached a copy of the Company's response to Consumer Advocate Interrogatory No. 2-9e to my testimony (Attachment 1). As this response illustrates, the Company also paid these fees to the firm of Thomas & Hutton:

1994	$31,559
1995	$50,129
1996	$ 0

For the reasons mentioned previously, I recommend that this cost be amortized over a five year period due to the unusual and extraordinary nature of the expense. As shown on Schedule 3 , this adjustment will reduce the Thomas & Hutton test year consulting fees by $40,103.

When the two adjustments previously described are considered in total, my proposal results in a reduction of $72,131 to the test year professional/consulting fees of $101,234.

Legal Fees

Q. Did the Company propose to adjust its test year legal fees?

A. No, it did not.

Q. Do you think an adjustment is in order?

A. Yes, I do. The test year legal fees should be normalized for ratemaking purposes. The test year legal fees amounted to $53,394, an amount considerably higher than the legal fees for the recent five year period. Shown below are the Company's legal fees for calendar years 1991 through 1995:

1991	$1,367
1992	$28,147
1993	$7,249
1994	$22,187
Test Year (1995)	$53,594

As shown, the test year legal fees are significantly higher those incurred during the previous four year period.

I have analyzed the Company's legal fees for the test year and have determined that there are two items which contribute to the abnormally high test year legal fees: $26,265 in legal fees associated with the Garretson vs. KIU proceeding, and $13,867 in legal costs associated with the Eugenia Avenue proceeding before this Commission in Docket No. 94-767-W.

Q. Would you please describe the Garretson vs. KIU proceeding?

A. According to the Company's response to Consumer Advocate Interrogatory No. 2-12, on July 20, 1994, a large house belonging to the Garretsons burned. The fire at the Garretsons spread next door and burned a large house owned by another homeowner. Both houses were insured and the insurance companies have paid between $3 to $4 million on the associated claims. However, the insurance companies, with the cooperation of the homeowners, have brought two lawsuits in the United States District Court for the District of South Carolina against the Company.

According to the Company's Audited Financial Statements for calendar year 1995, these lawsuits are just in the initial states of discovery so certainly other legal fees are going to be incurred. Therefore, it is my recommendation that the fees incurred during the test year be deferred and recovered when the lawsuits are ultimately settled in some manner.

Q. What is your total proposed adjustment to legal fees?

A. With the deferral of the Garretson legal expenses, the actual test year legal expense is reduced to $27,329. With this change, a normalized legal fees expense can be determined:

1991	$1,367
1992	$28,147
1993	$7,249
1994	$22,187
Test Year (1995)	$27,329
Average	$17,256

I recommend that the adjusted test year legal fees be normalized to reflect the average for the five year period of 1991 through 1995. As shown on Schedule 4, my proposed total adjustment reduces test year legal fees by $36,338.

Management Fee

Q. Does the Company pay a management fee to its parent company?

A. Yes, it does. During 1995, the Company paid Kiawah Resort Associates, L.P. a management fee of $100,000.

Q. What is your position regarding this management fee?

A. It is my position that this fee is excessive and that it should be adjusted for ratemaking purposes.

Q. Would you please explain why you believe that the management fee is excessive?

A. Initially, I oppose the inclusion of this management fee because the Company has not provided any support for how it was determined. In this regard, the Consumer Advocate requested this information in Consumer Advocate Interrogatory No. 2-16 and the Company responded that the data would be provided. However, it has not yet been provided. Without this type of information, the reasonableness of the management fee cannot be determined.

Beyond this, there seems to be considerable duplication between the services which are supposedly provided by the parent company and the direct costs incurred by the Company. For example, the Company has a manager, an assistant manager, and a controller on its payroll. During the test year, these three employees received salaries of $111,124. The Company also incurred audit and tax fees of $23,749.

I have attached to my testimony a copy of the Company's response to Consumer Advocate Interrogatory No. 2-16b (Attachment 2). A review of the services provided seem similar in nature to those which should be handled by the Company's in-house employees or by services provided by other outside professionals (i.e., those mentioned in the previous paragraph).

Attachment 2 also indicates that rate analysis assistance is one of the services provided by the management contract. Any such costs provided in connection with this proceeding should be included with rate case expense and normalized.

These are some of the concerns that need to be addressed before this management fee is adopted for ratemaking purposes.

Q. What level of management fees do you recommend be included in test year operating expenses?

A. For the reasons previously stated, it is my position that no management fees be allowed in this proceeding. The Company has not provided any support for the fees being paid to its parent company. Absent such data, there is no way to judge the reasonableness of these fees. Schedule 5 illustrates the appropriate adjustment.

Q. Are you aware that the Commission authorized fees of $36,000 in the Company's last rate proceeding?

A. Yes, I have reviewed the Commission's Order in the last rate proceeding (Order No. 92-1030 dated December 15, 1992). It is true that the Commission allowed management fees of $36,000, but it also indicated that the Company should provide data in future proceedings which would allow the reasonableness of such fees to be determined. As stated, this data was not provided.

Rate Case Expense

Q. Has the Company proposed an adjustment for rate case expense?

A. The Company proposes to increase its professional fees by $10,826 in order to reflect the amortized amount of rate case expense that the Commission allowed in its previous case.

Q. What is your position concerning the Company's proposed adjustment?

A. I oppose this adjustment, and I recommend that the Commission reject it. Although the Commission allows for the recovery of rate case expense incurred when seeking an increase in rates, the recovery should be based upon the actual costs associated with this proceeding, and not the previous one.

In this regard, it has been three years since the Company filed the last rate case in which it sought an increases in rates. In order to determine a normal level of rate case expenses, it would be appropriate to determine the rate case costs which have been incurred subsequent to the last rate case, including the costs associated with this proceeding, and to normalize those costs. However, since the Company has not provided the Commission with this data, it is not possible to quantify any reasonable adjustment.

Repair and Maintenance Expense

Q. Did the Company make any adjustments to its test year repair and maintenance expense?

A. Yes, the Company eliminated $19,226 in meters and materials and supplies. This is the amount associated with tap-in revenues and is properly charged to Contributions in Aid of Construction.

Q. Do you agree with the Company's proposed adjustment?

A. Yes, I agree with the elimination of the $19,226; however, the repair and maintenance expense should be adjusted further for ratemaking purposes.

Q. What additional adjustment do you propose?

A. The test year repair and maintenance expense amounted to $112,878, an amount considerably higher than the repair and maintenance expense for the recent five year period. Shown below are the Company's repair and maintenance expense for calendar years 1991 through 1995:

1991	$ 54,990
1992	$ 51,154
1993	$ 57,780
1994	$ 76,400
Test Year (1995)	$112,878
Average	$ 70,640

As shown, the test year repair and maintenance expense is significantly higher than the average for the five year period, as well as any of the other individual years during this five year period.

My analysis of the test year amounts provides an explanation as to why the test year expense is significantly higher than the expense incurred in the previous years shown. The test year expense includes $43,015 incurred to paint the St. John's Water Company elevated tank.

Tank painting expense is an expense that fluctuates significantly over time and proper accounting and ratemaking procedures require that it be spread over the time interval between tank paintings. The Company responded to Consumer Advocate Interrogatory No. 2-15b that the last painting was done prior to 1990, a period greater than five years ago.

Based on this information, it is my recommendation that the test year repairs and maintenance expense be normalized by considering the average expense incurred over the five year period of 1991 through 1995.

As shown on Schedule 6, the test year repair and maintenance cost is reduced by $32,111. As shown, the normalization was calculated by first eliminating the tap-in expenses which should be capitalized for ratemaking purposes.

Sludge Removal Adjustment

Q. Would you please describe the Company's proposed adjustment to sludge removal expense?

A. In the Application, the Company increased other operating expenses by $50,000. According to the Company, this amount approximates a three year average cost to remove sludge from holding cell #3. However, Company witness Clarkson testifies in his pre-filed testimony that based upon bids received subsequent to the filing of the application the estimate has been revised to $97,612.

Q. What is your position regarding this adjustment?

A. It is my position that the Commission should reject this proposed adjustment because it does not meet the known and measurable ratemaking standards.

The Company responded to Consumer Advocate Interrogatory No. 2-19 that no payments had been made, nor any invoices received, as of October 30, 1996. Historic test year amounts should only be adjusted by using amounts which have reasonable and definite characteristics, i.e., are known with some specificity. The Company's estimates do not meet this requirement and therefore the proposed adjustment should not be considered in this proceeding.

Beyond this, the Company has not provided the Commission with any support for its estimates. Moreover, if costs such as sludge removal which have not yet been paid ten months subsequent to the end of the test year are going to be considered, then it would also be appropriate to consider other changes such as the customer growth which has occurred subsequent to the end of the test year.

Depreciation Expense

Q. Would you please explain the Company's adjustment to its test year depreciation expense?

A. The test year depreciation expense was decreased by $32,323. This amount reflects a reduction of $33,284 relating to contributions in aid of construction, and an addition of $961 associated with the capitalization of meters, materials and supplies related to the tap-in expenses which were capitalized for ratemaking purposes.

Q. Do you agree with the Company's proposed adjustment?

A. I agree with the concept of the adjustment, but I don't agree with the amounts computed by the Company.

Q. Would you please explain the basis of your disagreement?

A. The $33,284 reduction proposed by the Company is simply a carry forward of the adjustment the Commission ordered in the last rate proceeding. In that proceeding, the rate base was determined as of December 31, 1991. Subsequent to that time, the Company has collected another $363,500 in tap-in revenues:

1992	$ 64,000
1993	86,250
1994	90,750
1995	122,500
Total	$363,500

This amount also needs to be transferred to Contributions in Aid of Construction and the depreciation associated with it needs to be eliminated for ratemaking purposes.

In addition, the Company has also expensed certain costs associated with the tap-in revenues which should be capitalized to rate base. The Company's adjustment only capitalized the 1995 amount, but did not capitalize the expenses for calendar years 1992 through 1994. The tap-in expenses incurred during these years also need to be capitalized, and when they are an additional depreciation expense adjustment will result.

Schedule 8 illustrates the appropriate adjustment. As shown, my proposed adjustment decreases depreciation expense by another $16,400.

Interest Synchronization

Q. Would you please explain your proposed interest synchronization?

A. Interest expense should be synchronized with the adjusted rate base so that there is a match between the two. My adjustment uses the same methodology as the Company except that I am recommending a lower rate base.

My recommended adjustment is shown on Schedule 9. As shown, I have used the capital structure and embedded cost of debt as of December 31, 1995. In addition, since my proforma interest is less than the per book interest, the income taxes will be increased as illustrated.

Rate Base

Q. What is your recommended rate base?

A. As shown on Schedule 10, my recommended rate base is $8,511,711.

Plant in Service

Q. Did the Company adjust its net plant in service?

A. Yes. The Company increased gross plant by $2,774,529 to recognize plant additions that according to it "have been set forth during 1996" (page D2-2 of Application). Additionally, it increased the plant by $19,226 to reflect the capitalization of the test year tap costs which were expensed on the books. The Company also increased the depreciation reserve to reflect the accumulated depreciation on the plant after one year of depreciation.

Q. Do you agree with the Company's proposed adjustment?

A. No, I do not. I agree with the capitalization of the tap costs which were previously expensed. Yet, as I discuss previously in my testimony the tap costs for calendar years 1992 through 1994 should also be capitalized since the revenues are now being classified as completed construction not classified.

The plant additions which the Company has used to increase rate base consists of CWIP which was completed as of the end of the test year, as well as CWIP which is projected to be completed during 1996 and beyond. It is my position that this is inappropriate for ratemaking purposes.

Q. Would you please explain this position?

A. The Company's financial report shows that the CWIP as of December 31, 1995 only amounted to $551,498. Therefore, the remainder of the plant items included by the Company had not been expended as of the end of the test year. It is my position that it is inappropriate to increase rate base with proposed CWIP which had not been completed prior to the end of the test year or even by the time this proceeding enters the hearing stage. This would only be appropriate if changes to the revenues and expenses which have occurred subsequent to the end of the test year are also taken into consideration. If these changes are not considered, then the operating income (operating revenues less operating expenses) does not match with the rate base, and this mismatching is not appropriate for ratemaking purposes.

In South Carolina, the rate base is established as of the end of the test year. As a result, the Commission typically considers adjustments such as growth in customers which have occurred during the test year so that the operating income will match with the year end rate base. If the Company's adjustment to include significant post test year rate base additions, in particular those which have not even been expended, is going to be considered for ratemaking purposes, then the operating income should likewise be adjusted. In this regard, the Company stated in its response to PSC Staff Data Request No. 1-2 that it expects to add another 60 taps during 1996.

Moreover, a significant portion of the Company's projected CWIP additions have not yet been expended. For example, the proposed adjustments includes $500,000 for the Eugenia Avenue Sewer project. As of the end of the test year, the Company had only expended $30,870 on this project, and the Company stated in response to the Kiawah Property Owners Group Inc.'s Interrogatory No. 1-8 that because of certain delays the contractor chosen to construct the extension was no longer available to do so. Thus, this project has not been completed and is not expected to be completed until after 1996.

Q. What adjustment do you recommend?

A. Only the CWIP which had been completed as of the end of the test year should be added to rate base. Additionally, the tap costs which were charged to expenses during calendar years 1992 through 1995 should also be added to rate base.

Depreciation Reserve

Q. How did you determine the adjustment to the depreciation reserve?

A. Previously in my testimony I discussed the recommended change to the test year depreciation expense. This adjustment captures the accrual of the annualized expense.

Completed Construction Not Classified

Q. How did you determine completed construction not classified (CIAC)?

A. In the last proceeding the Commission determined that CIAC amounting to $1,512,920 should be used to reduce rate base. Therefore, I used this amount to reduce rate base. In addition, I have increased the CIAC to reflect the tap-in revenues which were realized during calendar years 1992 through 1995. This is consistent with my recommendation to recognize the tap-in expenses in plant in service.

Q. Did the Company propose a similar adjustment to CIAC?

A. The Company reduced rate base with the $1,512,920 ordered by the Commission in the last proceeding, as well as with the tap-in revenues for the test year. However, it did not eliminate the tap-in revenues for calendar years 1992 through 1994. This is inappropriate as all the tap-in revenues should be recognized as an offset to rate base so that the ratepayer will receive a recognition of this non-investor source of funds in the form of lower depreciation and interest expense. Similarly, all of the tap-in expenses should be capitalized to rate base.

<u>Cash Working Capital</u>

Q. How did you determine cash working capital?

A. The lead-lag study is normally regarded as the most accurate method of determining cash working capital requirements. The purpose of this study is to determine the amount of cash required to pay expenses and taxes prior to (or after) the receipt of revenues. Revenue lags are computed in terms of the time interval between the provision of service and the collection of revenues associated with the services provided. Expense lags are computed based upon the time interval between the period when the expense was incurred and the date of payment for said expense. If the revenue lag exceeds the expense lag, then a positive cash working capital requirement results; if the expense lag exceeds the revenue lag, then a negative cash working capital requirement results. However, for utilities with smaller cash working capital requirements cash working capital is often determined on the basis of a formula method. However, when a formula method is used, it is critical that the ratio determined approximates the results of a lead-lag study, and in doing so provide a reasonable cash working capital requirement. The Company's formula method does not provide this result.

Q. Would you please explain why the Company's formula method does not provide a reasonable working capital requirement?

A. The Company's formula method simply considers 1/8th of the Company's operating expenses excluding depreciation and operating taxes. Whereas it is reasonable to allow for 1/8th of these expenses, because typically these expenses must be paid out before revenues are collected from the customers, it is unreasonable not to consider those operating expenses that are not paid until after the revenues are collected from the customers. For the Company, these expenses consist of property taxes and income taxes.

By not considering the property taxes and income taxes, the Company is determining a cash working capital requirement that only considers one-half of the cash working capital equation, the portion which increases cash working capital. This is improper and the Company should also consider the portion which decreases the cash working capital, because the revenues are being collected before these taxes have to be paid. I have recognized this other side of the cash working capital equation by offsetting the 1/8th formula used by the Company with a 1/4th allowance of property taxes and income taxes. The 1/4th ratio has long been known to be a reasonable representation of those expenses which are not paid until after the revenues are collected from the customer. My recommended cash working capital is shown on Schedule 10.

Customer Growth

Q. Why is a customer growth adjustment appropriate?

A. In order to produce an appropriate revenue requirement, the test year operating income must be measured against the rate base which generated it. Stated another way, the operating income should match, or be consistent with, the rate base which is being used to generate the operating income. When a test period is based upon a 12 month accounting period and the rate base is based upon the average investment during this 12 month period, the desired consistency is present. However, a mismatch occurs when the rate base is valued at the end of the test period, unless there has been no measurable growth during the test period.

This is the situation in the instant proceeding. The Company's rate base is determined as of December 31, 1995, but the test year revenues are realized over the 12 month period ending the same date. Therefore, a mismatch occurs.

Q. What can be done to eliminate the mismatch between operating income and rate base?

A. The operating income should be adjusted to incorporate the revenues and expenses which would be realized on the basis of the actual investment at year end. A reasonable method of making this determination, and to eliminate the mismatch, is to annualize revenues and the associated expenses to reflect the growth in customers by comparing the year-end customer levels to the average customer levels during the test year. By using customer levels at year end, the revenue requirement computation will consider the revenues associated with the customers at year-end as well as the investment required to provide service to these customers.

Q. How the Company adjusted for customer growth?

A. The Company has used a factor which is determined on the basis of the growth between average customers and year end customers. This formula, if applied correctly, might eliminate the mismatch of operating income with rate base previously discussed; however, the Company does not apply it correctly.

The Company simply multiplies the formula against its operating income thereby making the assumption that all of the Company's expenses are going to increase proportionately to the increase in revenues. Yet, this is not the case. There are certain expenses which vary with usage and customers, and which should be adjusted when the revenues are adjusted. Although there could be others, typically these expenses are purchased water, purchased power, chemicals, and customer billing expenses. If the Company believes that there are other expenses which change directly as a result of changes in usage and customers, the burden should be on the Company to support its position. Only these expenses should be adjusted in order to match with the corresponding adjustments to revenues, not all the expenses as adjusted by the Company. For example, the Company's computation assumes that salaries and wages are going to grow in proportion to the growth in revenues which are generated from a growth in customers. Eventually, continued growth in customers will ultimately lead to employees being added to meet this growth. However, it is absurd to conclude that labor will grow in proportion to the growth in revenues and customers.

Q. How have you adjusted for customer growth?

A. I have determined the impact on operating income which actually exists as a result of growth in customers. As shown on Schedule 11, I have reduced operating revenues with those operating expenses which increase as a result of adding customers: purchased water, purchased power, chemicals, and postage. This generates the net income which is actually impacted by a growth in customers. To this amount then, I have applied the 1.8% factor determined by the Company to measure the growth in year end customers over average customers. This methodology measures the true growth in net income rather than the growth determined by the Company which assumes that all the expenses are going to grow proportionately to the growth in revenues.

Q. Does this conclude your testimony?

A. Yes, it does.

APPENDIX 1

PHILIP E. MILLER

Mr. Miller is a Senior Accountant and an expert accounting witness with Riverbend Consulting specializing in regulatory matters. During the past twenty-nine years, he has testified as an expert in more than 300 rate proceedings in numerous states on virtually all aspects of public utility accounting and ratemaking. Mr. Miller has served as a Chief Accountant at a regulatory agency, a Technical Advisor to a consumer advocate, and a Chief Accountant/Treasurer at a gas utility.

EDUCATION

B.S. in Business Administration- Major: Accounting	The Ohio State University

EMPLOYMENT

Present	Senior Accountant, J.W. Wilson & Associates, Inc.
1980-1992	President, Riverbend Consulting
1977-1980	Technical Advisor, Office of the Consumers' Counsel, State of Ohio
1971-1977	Director, Chief Accountant, Public Utilities Commission of Ohio
1971	Treasurer, Chief Accountant, National Gas & Oil Company
1967-1971	Senior Accountant, Columbus Southern Power

PAPERS & PUBLICATIONS

"What Techniques Have Proven Successful in Locating and Obtaining Consultants and Technical Staff", State Utility Consumer Advocates Conference; June 19-20, 1979

"Rate Reform Proposals Can be Measured by Actual Data", Proceedings of the Second NARCU Biennial Regulatory Information Conference; September 1989

"Consumer Effectiveness", Free Enterprise Workshop, Rio Grande College; June 21, 1984

"Edison Electric Institute (EEI) Dues: Ratepayers' or Stockholders' Responsibility", 5th Annual Public Utilities Conference; September 11-13, 1985

"What Can OCC and the State of Ohio do to Encourage Ohio Consultants to Bid and Successfully Obtain OCC Contracts", 1977-1987 A Decade of Advocacy Conference; April 2-3, 1987

"The 1986 Tax Act: Its Impact on Utilities and Regulation", 1987 Western Conference of Public Service Commissioners; June 7-10, 1987

EXPERT TESTIMONY IN UTILITY RATE PROCEEDINGS

Utility	Case/Docket No.	Filing Date
River Gas	76-815-GA-AIR	July 1977
Ohio Edison	77-554-EL-AIR	January 1978
Ohio Edison	77-869-HT-AAM	January 1978
Toledo Edison	76-174-EL-AIR	April 1978
Dayton Power & Light	78-92-EL-AIR	December 1978
Ohio Power Company	78-676-EL-AIR	January 1979
Columbus & Southern	78-1438-EL-AIR	Sept. 1979
Ohio Edison	78-1567-EL-AIR	November 1979
East Ohio	79-535-GA-AIR	April 1980
Ohio Power	79-234-EL-FAC	June 1980
Ohio-American Water	79-1343-WW-AIR	October 1980
River Gas	80-45-GA-AIR	November 1980
Ohio Edison	80-141-EL-AIR	November 1980
Dayton Power & Light	80-826-EL-AIR	Not Available
Ohio Power	80-367-EL-AIR	January 1981
Dayton Power & Light	80-687-EL-AIR	April 1981
Mountain Bell Telephone	943	April 1981
Public Service Co. of New Mexico	1602	May 1981
Dayton Power & Light	80-1087-GA-AIR	August 1981
Lake White Water Works	80-744-WW-AIR	August 1981

Cleveland Elect. Ill.	81-41-HT-AIR	October 1981
Dayton Power & Light	81-21-EL-AIR	November 1981
Cleveland Elect. Ill.	81-146-EL-AIR	December 1981
General Telephone	81-383-TP-AIR	January 1982
Columbia Gas of PA	R-811627	February 1982
Ohio Power	81-782-EL-AIR	April 1982
East Ohio	81-970-GA-AIR	May 1982
Columbus & Southern	81-1058-EL-AIR	June 1982
Masury Water	81-999-WW-AIR	June 1982
Columbia Gas of Ohio	80-1155-GA-AIR	August 1982
South Carolina Electric & Gas Company	82-239-G	August 1982
Cincinnati Bell Tele.	81-1338-TP-AIR	Sept. 1982
Ohio Water Service Co.	81-1467-WW-AIR	October 1982
South Carolina Electric & Gas Company	82-240-E	January 1983
Florida Power & Light	820097-EU	March 1983
Dayton Power & Light	82-517-EL-AIR	April 1983
East Ohio Gas	82-901-GA-AIR	May 1983
Ohio Edison	82-1025-EL-AIR	June 1983
Ohio Water Service	83-47-WW-AIR	August 1983
South Carolina Electric & Gas Company	83-217-G	Sept. 1983
Ohio Power	83-98-EL-AIR	Sept. 1983
Duke Power	83-302-E	November 1983
Columbia Gas of Ohio	83-392-GA-AIR	February 1984
Columbia Gas of Ohio	83-545-GA-AIR	March 1984
Columbia Gas of Ohio	83-584-GA-AIR	March 1984
Columbia Gas of Ohio	83-967-GA-AIR	March 1984
Ohio Edison	83-1130-EL-AIR	April 1984
Terraceway Service	83-267-S	April 1984

Midlands Utility	83-344-S	April 1984
Columbia Gas of Ohio	83-1301-GA-AIR	May 1984
Puget Sound	U-83-54	May 1984
People's Natural Gas	83-495-G	June 1984
Piedmont Utilities	83-499-S	July 1984
Fripp Island	84-55-S	Sept. 1984
Ohio Power Company	84-11-EL-EFC	Sept. 1984
Ohio Water Service	84-392-WW-AIR	November 1984
Central Maine Power	84-120	December 1984
Columbia Gas of Ohio	84-67-GA-AIR	January 1985
San Diego Gas & Electric	84-012-015	April 1985
Columbia Gas of Ohio	83-1519-GA-AIR	May 1985
Columbia Gas of Ohio	84-552-GA-AIR	June 1985
Columbia Gas of Ohio	84-754-GA-AIR	July 1985
Duke Power	85-78-E	July 1985
Cincinnati Bell Tele.	84-1272-TP-AIR	August 1985
Columbia Gas of Ohio	84-1102-GA-AIR	August 1985
Columbus & Southern Ohio	85-02-EL-EFC	Sept. 1985
Carolina Water Service	85-169-W/S	Sept. 1985
Hawaiian Telephone	5411	October 1985
Central Telephone	84-1431-TP-AIR	November 1985
Masury Water	85-290-WW-AIR	January 1986
Puget Sound	U-85-53	January 1986
Cleveland Elect. Ill.	85-675-EL-AIR	February 1986
Arizona Public Service	U-1345-85-156	February 1986
Central Maine Power	85-212	April 1986
Chillicothe Telephone	85-995-TP-AIR	July 1986
ALLTEL Ohio	86-60-TP-AIR	Sept. 1986
Carolina Water Service	86-220-W/S	October 1986
Louisiana Power & Light	U-16945	December 1986

Arizona Public Service	U-1345-85-367	February 1987
Realtec Incorporated	86-391-W/S	March 1987
South Carolina Electric & Gas Company	87-43-E	May 1987
Carolina Power & Light	87-7-E	June 1987
Newport Electric	1872	July 1987
South Carolina Electric & Gas Company	87-227-G	Sept. 1987
South Carolina Electric & Gas Company	87-332-T	October 1987
South Carolina Electric & Gas Company	87-10-E	November 1987
Lockhart Power Company	87-435-E	December 1987
Generic Proceeding to Study Impact of TRA-86	87-456-W/S	December 1987
GTE North	87-1307-TP-AIR	May 1988
Carolina Power & Light	88-11-E	June 1988
Central Power & Light	7560	July 1988
Alpine Utilities	88-56-S	July 1988
Toledo Edison	88-105-EL-EFC	October 1988
Midlands Utility	88-237-S	January 1989
Carolina Water Service	88-241-W/S	March 1989
South Carolina Electric & Gas Company	88-681-E	April 1989
Pacific Gas & Electric	88-12-005	April 1989
Columbia Gas of Ohio	88-1011-GA-CMR	April 1989
Central Power & Light	8646	June 1989
South Carolina Electric & Gas Company	89-245-G	Sept. 1989
Columbia Gas of Ohio	89-943-GA-CMR	December 1989
South Carolina Electric & Gas Company	89-543-E	January 1990

Ohio Edison	89-1001-EL-AIR	March 1990
United Utility Companies	89-602-W/S	May 1990
Wild Dune Utilities	89-601-W/S	May 1990
Carolina Water Service	89-610-W/S	June 1990
Wildewood Utilities	89-426-S	August 1990
Cincinnati Gas & Elect.	90-390-GA-AIR	October 1990
Columbia Gas of Ohio	90-17-GA-GCR	November 1990
Heater of Seabrook	90-124-W/S	January 1991
Fripp Island	90-559-S	March 1991
Harbor Island	90-560-S	March 1991
Cincinnati Gas & Elect.	91-03-EL-EFC	April 1991
TCU, Inc.	90-287-W/S	April 1991
Midlands Utility, Inc.	90-528-S	April 1991
Heater Utilities	91-096-W	August 1991
Columbia Gas of Ohio	91-195-GA-AIR	August 1991
Duke Power	91-216-E	Sept. 1991
Piedmont Natural Gas	91-141-G	Sept. 1991
Woodland Utilities	91-237-S	Sept. 1991
Columbus Southern Power	91-418-EL-AIR	December 1991
CUC, Inc.	91-041-W/S	January 1992
Hartwell Utilities	90-781-W/S	January 1992
Upstate Heater Utilities	91-095-W	February 1992
South Carolina Electric & Gas Company	92-023-R	May 1992
Mountaineer Gas Company	92-0063-G-42T	July 1992
Realtec, Inc.	91-682-W/S	July 1992
United Telephone	92-271-C	October 1992
Heater of Seabrook	91-627-W/S	October 1992
Heater Utilities	92-031-W	November 1992

South Carolina Electric & Gas Company	92-619-E	March 1993
Carolina Water Service	91-641-W/S	March 1993
Cincinnati Gas & Elect.	92-1464-EL-AIR	April 1993
Bangor-Hydro Electric	93-062	August 1993
Western Reserve Tele.	92-1525-TP-CSS	August 1993
Western Reserve Tele.	93-230-TP-ALT	November 1993
GTE South	93-504-C	February 1994
Heater Utilities, Inc.	93-720-W	April 1994
Heater of Seabrook	93-737-W/S	May 1994
Southern Bell	93-504-C	August 1994
Upstate Heater Utilities	94-304-W	November 1994
Indianapolis Power & Light Company	39938	April 1995
Blue Ribbon Water Corp.	93-636-W/S	April 1995
Southern Bell	95-862-C	August 1995
South Carolina Electric & Gas Company	95-1000-E	October 1995
The Cleveland Electric Illuminating Company	95-300-EL-AIR	December 1995
Toledo Edison Company	95-299-EL-AIR	December 1995
Citizens Utilities Company	E-1032-95-417, Et. Al.	July 1996

ATTACHMENTS

Attachment 1

Attachment 2

KIAWAH ISLAND UTILITY, INC.
RESPONSES TO CONSUMER ADVOCATE GROUP 2

Item 2-9e

The engineering costs for fire related studies are as follows:

Year	Payee	Amount
1994	Gage Babcock	$17,453.12
	C.F. Vandenbulk	3,611.25
	Thomas & Hutton	31,559.10

		$52,623.47
1995	Gage Babcock	$40,035.35
	Thomas & Hutton	50,129.37

		$90,164.72
1996	Gage Babcock	$2,300.70

		$2,300.70

STATE OF SOUTH CAROLINA)
) MANAGEMENT SERVICES AGREEMENT
COUNTY OF CHARLESTON)

THIS AGREEMENT entered into as of the 1st day of January 1993 by and between KIAWAH RESORT ASSOCIATES, L.P. ("KRA") and KIAWAH ISLAND UTILITY, INC. ("UTILITY").

BACKGROUND OF AGREEMENT

1. UTILITY owns and operates the water and wastewater company which furnishes water and wastewater services to Kiawah Island, South Carolina.

2. UTILITY is a wholly-owned subsidiary of KRA.

3. UTILITY does not have the personnel and management capabilities to perform many of the management functions necessary for the operation of the UTILITY. The personnel employed by UTILITY are, for the most part, technical personnel who are experienced in the water and wastewater services industry, rather than general management services.

4. UTILITY desires to enter into a Management Services Agreement with KRA, whereby KRA will provide to UTILITY general management services, particularly as they relate to policy, financial and personnel matters.

5. KRA has agreed to provide such services for the sum of $100,000.00 annually.

NOW, THEREFORE, KRA agrees to perform the following services:

A. Budget preparation and review.

B. Financial statement preparation and review.

C. Daily operations - management overview.

D. Rate analysis assistance.

E. Plant expansion/capital additional analysis and review.

F. Forecasting - operations and cash flow.

G. Personnel review - policy and performance.

H. Cash disbursement - review and approval.

I. Payroll disbursement - review and approval.

J. Policy review and management.

K. Secretarial assistance when needed.

L. Coordination with St. John's Water Company in policy matters.

M. Bank relations and financial management.

6. This Agreement will commence on the date set forth above and continue on a month-to-month basis until such time as either party gives the other thirty (30) days written notice of its desire to terminate the Agreement.

7. This Agreement may not be assigned without the written permission of both parties.

IN WITNESS WHEREOF, the parties have set their Hands and Seals as of the day and year first above written.

WITNESSES:

Wendy Roach

Katherine M. Brown

Marie Roper

KIAWAH RESORT ASSOCIATES, L.P. (SEAL)

By: D&W Investments, Inc.
Its Managing Partner

By: ______________________
Charles S. Way, Jr.
Its President

By: ______________________
Betty R. Crow
Its Secretary

KIAWAH ISLAND UTILITY, INC. (SEAL)

By: Becky J. Dennis
Its: Manager

SCHEDULES

Kiawah Island Utility, Inc.
Docket No. 96-168-W/S
Adjusted Operating Income
For the Test Year Ended December 31, 1995

		Company Adjusted (a)	Adjustments (b)	CA Adjusted (c)
1	**Operating Revenues**	$2,650,861		$2,650,861
2	**Operating Expenses**			
3	Purchased Water	924,403		924,403
4	Salaries and Benefits	367,301		367,301
5	Management Fee	100,000	($100,000)	0
6	Fuel and Electricity	109,189		109,189
7	Repairs and Maintenance	93,652	(32,111)	61,541
8	Other Operating Expenses	383,652	(122,505)	261,147
9	Depreciation and Amortization	293,971	(17,361)	276,610
10	Property Taxes	109,025		109,025
11	Income Taxes	12,000	16,051	28,051
12	Total Operating Expenses	2,393,193	(255,926)	2,137,267
13	**Net Operating Income**	257,668	255,926	513,594
14	**Customer Growth Factor**	2,998	25,849	28,847
15	**Net Operating Income for Return**	$260,666	$281,775	$542,441
16	**Operating Margin**	-10.07%		7.58%

Sources:
(a) Company Exhibits A and D
(b) Schedule 2
(c) (a)+(b)

Kiawah Island Utility, Inc.
Docket No. 96-168-W/S
Adjusted Operating Income

Line	Source
5	Schedule 5
7	Schedule 6
8	Schedules 3, 4 & 7
	Company Exhibit D-2
9	Schedule 8
11	Schedule 9
14	Schedule 11

Schedule: 3

Kiawah Island Utility, Inc.
Docket No. 96-168-W/S
Professional Fees

1	Gage-Babcock Consulting Fees (a):	
2	Test Year Amount	$40,035
3	Amortization over Five Years 2/Five Years	8,007
4	Less: Test Year Amount	40,035
5	Adjustment 3-4	($32,028)
6	Thomas & Hutton Consulting Fees (a):	
7	Test Year Amount	$50,129
8	Amortization over Five Years 7/Five Years	10,026
9	Less: Test Year Amount	50,129
10	Adjustment 8-9	($40,103)
11	Total Adjustment 5+10	($72,131)
12	Company's Proposed Adjustment (b)	(46,790)
13	Additional Adjustment 11-12	($25,341)

Sources:
(a) Company's Responses to CA Interrogatories 2-9 and 2-10
(b) Company Schedule D-1

Schedule: 4

Kiawah Island Utility, Inc.
Docket No. 96-168-W/S
Legal Fees

1	Test Year Legal Fees (a)	$53,594
2	Deferral of Garretson Lawsuit (a)	(26,265)
3	Adjusted Test Year Legal Fees 1-2	27,329
4	Average Legal Fees for 1991-1995 (b)	17,256
5	Normalization Adjustment 4-3	(10,073)
6	Total Legal Fee Adjustment 2+8	($36,338)

Sources:
(a) Company's Response to CA Interrogatory 1-7
(b) Refer to Text

Schedule: 5

Kiawah Island Utility, Inc.
Docket No. 96-168-W/S
Management Fees

1	Proposed Management Fee	$0
2	Test Year Management Fee	100,000
3	Adjustment 1-2	($100,000)

Sources:
(a) Refer to Text
(b) Company Exhibit A

Schedule: 6

Kiawah Island Utility, Inc.
Docket No. 96-168-W/S
Repairs and Maintenance Expense

1	1991 Expense Excluding Tap-in Expenses (a)	$44,988
2	1992 Expense Excluding Tap-in Expenses (a)	51,154
3	1993 Expense Excluding Tap-in Expenses (a)	48,326
4	1994 Expense Excluding Tap-in Expenses (a)	69,584
5	1995 Expense Excluding Tap-in Expenses (b)	93,652
6	Total Expenses !+2+3+4+5	307,704
7	Five Year Average 6/Five	61,541
8	Less: Test Year Amount	93,652
9	Adjusted Test Year 7-8	($32,111)

Sources:
(a) Company's Response to Consumer Advocate Interrogatory No. 2-5
(b) Company Exhibit A and D-2

Kiawah Island Utility, Inc.
Docket No. 96-168-W/S
Rate Case Expense

1	Elimination of Company's Proposed Expense (a)	($10,826)

Sources:
(a) Company Exhibit D

Schedule: 8

Kiawah Island Utility, Inc.
Docket No. 96-168-W/S
Depreciation Expense

1	Tap-in Expenses To Be Capitalized For Calendar	
2	Years 1992 Through 1995 (a)	$35,496
3	Tap-in Revenues Realized During Calendar Years	
4	1992 Through 1995 (b)	363,500
5	Net Change 2-4	(328,004)
6	Average Depreciation Rate (c)	5.00%
7	Reduction to Test Year Depreciation 5*6	(16,400)
8	Less: 1995 Tap-in Depreciation Previously	
9	Considered in Company's Adjustment (c)	961
10	Additional Depreciation Adjustment 7-9	($17,361)

Sources:
(a) Company's response to Consumer Advocate Interrogatory Nos. 2-2 & 2-5
(b) Company's response to PSC Staff Data Request No. 1-12
(c) Company's response to Consumer Advocate Interrogatory No. 1-8

Schedule: 9

Kiawah Island Utility, Inc.
Docket No. 96-168-W/S
Interest Synchronization

1	Rate Base (a)	$8,471,469
2	Embedded Cost of Debt (b)	4.03%
3	Interest Expense 1*2	341,400
4	Per Book Interest (b)	388,610
5	Reduction to Per Book Interest 4-3	47,210
6	Tax Rate	34.00%
7	Income Tax Impact 5*6	$16,051

Sources:
(a) Schedule 10
(b) Company Exhibit D, Schedule 4

Schedule: 10

Kiawah Island Utility, Inc.
Docket No. 96-168-W/S
Rate Base

1	Net Plant in Service Per Books (a)	$9,530,992
2	Tap-in Expenses To Be Capitalized For Calendar	
3	Years 1992 Through 1995 (b)	35,496
4	Depreciation Reserve (c)	48,723
5	CWIP (a)	551,499
6	Completed Construction Not Classified	
7	Balance as of December 31, 1991	1,512,920
8	Tap-in Revenues Realized During Calendar Years	
9	1992 Through 1995 (b)	363,500
10	Cash Working Capital (d)	181,178
11	Rate Base 1+3-4+5-7-9+10	$8,471,469

Sources:
(a) Company Exhibit D
(b) Schedule 8
(c) Schedule 8 and Company Exhibit D
(d) 1/8th Operating Expenses Excluding Depreciation and Taxes
Less: 1/4th Operating Taxes

Schedule: 11

Kiawah Island Utility, Inc.
Docket No. 96-168-W/S
Customer Growth Adjustment

1	Adjusted Operating Revenues (a)	$2,650,861
2	Less: Expenses Directly Related to Growth in	
3	Customers and Revenues (b):	
4	Purchased Water	924,403
5	Purchased Power	109,189
6	Chemicals	1,754
7	Freight and Postage	12,927
8	Operating Income Related to Growth in Customers	1,602,588
9	Customer Growth Factor (c)	1.80%
10	Customer Growth Adjustment 8*9	$28,847

Sources:
(a) Schedule 1
(b) Company's 1995 Annual Reports Filed with the PSC
(c) Company Exhibit D